Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Schools and Libraries Universal Service Support Mechanism	)	**CC Docket No. 02-6**
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	)	

REPLY COMMENTS OF HAYES E-GOVERNMENT RESOURCES, INC.

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I. INTRODUCTION AND SUMMARY

Hayes E-Government Resources, Inc. ("Hayes"), by its undersigned counsel, submits these reply comments in the above-referenced E-rate proceeding. Hayes provides telecommunications and Internet access services to customers in the State of Florida. Hayes has been an active participant in the E-rate program since 1999, and, as such, is pleased to have this opportunity to respond to the comments submitted in this proceeding regarding proposed changes to the E-rate program.

Hayes' reply comments are focused on four areas of the program: (1) the rules for the return of inappropriately distributed funds; (2) the Form 470 competitive bidding requirements; (3) the processing timeframes for E-rate appeals applications; and (4) the requirements for applicants to "guarantee" matching funds to pay the undiscounted portion of a funding request.

First, Hayes strongly agrees with the majority of commenters that service providers should not bear sole liability for the return of improperly distributed funds. Rule changes that would require the return of funds from the applicant in situations where the applicant is at fault for the improper distribution, as well as changes that limit the period within which improperly

distributed funds may be sought, are urgently needed in order to allocate liability for improperly distributed funds in a more equitable manner.

Second, Hayes proposes that the Commission eliminate the Form 470 competitive bidding process for those applicants who employ a competitive bidding process under state or local procurement law. The Form 470 competitive bidding process, rather than being a help, has become a hindrance to participants seeking E-rate funding for telecommunications and Internet access services. Thus, the Commission should instead allow applicants to certify compliance with applicable state and/or local bidding requirements as a way of ensuring that competition and cost-effective goals are met.

Third, the practical result of the current lengthy processing timeframes for E-rate applications and appeals is that applicants are not always able to utilize funding requests even if the funding is ultimately granted. Hayes believes that a maximum six-month processing timeframe for applications and appeals would greatly improve the utilization of E-rate funding by successful E-rate applicants and improve the overall efficiency of the program.

Finally, Hayes submits that applicants whose budgets have not yet been approved by the appropriate state or local government at the time E-rate applications are due should be allowed to defer their "guarantee" of matching funds for the undiscounted portion of their request as a condition of any E-rate funding grant. This clarification will help to ensure that qualified schools and libraries are afforded a full opportunity to take advantage of E-rate funding, namely the ability to obtain affordable telecommunications and Internet access services.

II. MORE EQUITABLE PROCEDURES SHOULD BE ADOPTED FOR RETURN OF INAPPROPRIATELY DISTRIBUTED FUNDS

Under current E-rate program rules, reimbursement for inappropriately distributed funds is sought from the service provider, regardless of whether the service provider was at fault for the inappropriate disbursement. An overwhelming majority of the commenters who addressed this issue agree that reform of this policy is urgently needed.[1] Like many commenters, Hayes believes that it is patently unfair and inequitable for service providers to bear sole liability for inappropriately distributed funds.[2] This is particularly true in situations where the improper disbursement is not due to the actions of the service provider.

As other commenters have pointed out, in situations in which the applicant is at fault for the inappropriate funding distribution, the current rules do not provide any incentive for the applicant to reimburse the service provider for the disbursement.[3] Importantly, even if the service provider chooses to jeopardize its good will with the applicant and seek reimbursement, as a practical matter, the service provider is unlikely to succeed in obtaining reimbursement for the inappropriately distributed funds from the school or library. One reason for this is that many service providers are not able to negotiate the terms contained in the service contracts, and, thus, may not be allowed to include a provision for reimbursement of inappropriately distributed funds

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[1] *See* Comments of SBC Communications ("SBC") at 3-10; Comments of BellSouth Corporation ("BellSouth") at 3-6; Comments of the Consortium for School Networking and International Society for Technology in Education ("ITSE") at 8; Comments of Cox Communications, Inc. ("Cox") at 8-10; Comments of General Communications, Inc. ("GCI") at 5-7; Comments of Kellogg & Sovereign Consulting, LLC at 12; Comments of National Telecommunications Cooperative Association at 4-5; Comments of On-Tech at 13-15; Comments of Qwest Communications International Inc. ("Qwest") at 9-11; Comments of Sprint Corporation at 7-9; Comments of State E-Rate Coordinators' Alliance at 9-10; Comments of Verizon at 2-10; Comments of Greg Weisiger ("Weisiger") at 15-16; and Comments of WorldCom, d/b/a MCI ("MCI") at 4.

[2] *See* Comments of SBC at 4; Comments of GCI at 6; Comments of Qwest at 10; and Comments of Verizon at 3.

in the contract with the school. Rather, many service providers are forced to sign the service contract presented by the applicant or otherwise not be allowed to provide service to the applicant. Additionally, reimbursement from a school or library is improbable because funding for such entities is usually allocated through a state or local budget process that likely would not approve additional funding devoted to E-rate reimbursement. State and local officials, without a specific mandate from the federal government, have little incentive to provide funding for reimbursement. This problem is particularly exacerbated by the current economic constraints under which most state and local budgets operate.

Indeed, not only are the current reimbursement procedures for inappropriately distributed funds unfair and inequitable, they also provide a strong disincentive for participation by smaller service providers who cannot afford to bear sole responsibility for the return of distributed funds. This disincentive is directly contrary to the program's goals for an effective competitive bidding process. Likewise, as other commenters mentioned, the current procedures also fail to create an incentive for applicants to comply with E-rate program requirements when they are not held liable for funds improperly distributed due to their non-compliance.[4] Again, this incentive is completely inconsistent with the Commission's and the Universal Service Administrative Company's ("USAC's") efforts to curb waste, fraud and abuse in the program.

The current reimbursement procedures for inappropriately-distributed funds are also inconsistent with federal case law and the policies articulated in USAC's Service Provider

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3 *See* Comments of SBC at 4; Comments of Cox at 9; and Comments of Verizon at 3.

4 *See* Comments of SBC at 4; and Comments of Qwest at 11.

Manual.[5] Specifically, based in part on the policies in USAC's Service Provider Manual, the United States Court of Appeals for the First Circuit found that funds distributed as part of the E-rate program are the property of the applicant, not the service provider.[6] Rather than having a property interest in the funding distribution, the First Circuit found that the service providers merely act as a "vehicle" to deliver the funding to the applicant.[7] If the distributed funding is the property of the applicant, then the service providers should not be responsible for reimbursement of those funds. In other words, the program's policy of seeking reimbursement from only the service provider is not consistent with the First Circuit's interpretation of federal law that the service provider is merely a vehicle for deliverance of the distributed funds to the applicant.[8]

Accordingly, Hayes strongly supports the position of many commenters that the program rules should be changed to mandate that improperly-distributed funds be obtained from the applicant, and not from the service provider, in situations where the improper distribution was due to actions of the applicant.[9] Additionally, Hayes also agrees with other commenters that a statute of limitations period, such as two years, should be adopted for seeking return of inappropriately distributed funds.[10] While Hayes understands the Commission's desire to correct disbursement mistakes, the uncertainty that is created by an unlimited reimbursement

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5 *See In re Lan Tamers, Inc.*, 329 F.3d 204 (1st Cir. 2003); *see also* USAC's Service Provider Manual, Chapter 9, *available at* www.sl.universalservice.org/vendor/manual.

6 *Lan Tamers*, 329 F.3d at 207-208.

7 *Id.* at 211-212.

8 *See also* Comments of SBC at 3-4 (citing to *Changes to the Board of Directors of the National Exchange Carrier Association, Inc., Federal-State Joint Board on Universal Service*, CC Docket Nos. 97-21 and 96-45, 15 FCC Rcd 22,975 (2000)).

9 *See* Comments of SBC at 5-6; Comments of BellSouth at 5; Comments of Cox at 9; Comments of Qwest at 10; and Comments of Verizon at 4-5.

10 *See* Comments of Cox at 9-10; Comments of the Education and Libraries Network Coalition at 8; and Comments of ITSE at 8.

(Cont'd)

period harms the process more than it benefits it. Without a statute of limitations period, a funding commitment letter does not, in fact, represent a commitment, and the inability to rely on a commitment jeopardizes the integrity of the entire program.

III. THE COMMISSION SHOULD ELIMINATE THE FORM 470 COMPETITIVE BIDDING PROCESS FOR APPLICANTS THAT CAN CERTIFY COMPLIANCE WITH APPLICABLE STATE OR LOCAL COMPETITIVE BIDDING REQUIREMENTS

It is clear from the comments that six years of experience has demonstrated that the Form 470 competitive bidding process is not working as well as the Commission intended. Instead of fostering competition and lowering prices as the Commission had hoped, over the years the competitive bidding rules have become increasingly complicated to the extent that now, unfortunately, they serve as impediment to qualified applicants seeking E-rate funding. Indeed, as another commenter pointed out, an applicant's inability to comply with the competitive bidding rules is, by USAC's own admission, one of the primary reasons for denial of funding under the E-rate program.[11] Accordingly, these rules need to be reassessed by the Commission to determine the value of these requirements and their contribution to the efficiency and effectiveness of the E-rate program.

Importantly, it has been Hayes' experience that the Form 470 process and related requirements create a great deal of confusion for applicants because the applicants must also comply with state and/or local procurement laws. Often the state and local procurement processes and requirements are not the same as, and even may conflict with, the E-rate's competitive bidding requirements. Thus, an applicant is forced to spend additional precious

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[11] *See* Initial Comments of Illinois State Board of Education at 7.

resources to determine how to modify a state's existing bid selection process in a way to ensure that it is both in compliance with state and/or local procurement laws as well as the E-rate competitive bidding requirements. Given the complexity of the E-rate competitive bidding rules, this may be a time consuming process for applicants that otherwise are much more familiar with utilizing a bidding process that complies with state and/or local procurement law.

In addition to necessitating the establishment of a modified or entirely new bidding process outside of a state's standard process, the current E-rate competitive bidding requirements result in inefficiencies in the E-rate process. For example, under the current E-rate competitive bidding rules, applicants must separately consider the pricing for E-rate eligible services and use price as the primary factor in selecting a service provider.[12] Applicants, are not required, however, to employ a separate bidding process for eligible and ineligible services, nor are they prohibited from selecting one service provider for both eligible and ineligible services. Logically, many applicants conduct one bidding process for eligible and ineligible services because of the efficiencies that result from working with one service provider instead of two. However, in an attempt to be the lowest-priced bidder for E-rate eligible services, a service provider could bid below market pricing for E-rate eligible services, while inflating its pricing for non-eligible services. Because the competitive bidding rules require price of eligible services to be the primary factor in selecting a winning bid, an applicant could find itself in a situation where it must select the service provider who bid the lowest price for the E-rate eligible services, even though the prices of that bidder are actually below market value for the eligible services and

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[12] *See Request for Review of the Decision of the Universal Service Administrator by Ysleta Independent School District, El Paso, Texas, et al*., CC Docket Nos. 96-45 and 97-21, Order, at ¶¶ 44-51 (rel. Dec. 8, 2003).

above market value for the non-eligible services. While this result might minimize the amount of E-rate support provided to the applicant, it would not minimize the applicant's overall cost of purchasing services and, thus, would contrary to the goals of the program to reduce the costs schools and libraries incur to provide their students and patrons access to advanced telecommunications services.[13]

Moreover, as evidenced by the comments submitted in proceeding, it appears that the current E-rate competitive bidding requirements do not assist applicants in obtaining affordable telecommunications and Internet services, but rather serve as an impediment to this goal. Accordingly, Hayes suggests that the Commission eliminate the Form 470 competitive bidding process for applicants that can certify compliance with applicable state or local competitive bidding requirements.[14] By requiring compliance with a state or local competitive bidding requirements, the Commission will have assurances that the its goals of competition and cost-effectiveness are continuing to be fulfilled even in the absence of specific E-rate bidding requirements. While it is likely that most applicants will have a state or local competitive bidding process that they can follow, for those applicants whose applicable state or local procurement laws do not contain a competitive bidding process, such applicants could be required to follow a streamlined Form 470 competitive bidding process. In other words, a streamlined Form 470 competitive bidding could act as a "default" in those rare situations where

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[13] Hayes submits that this result would be even more likely to occur if the Commission were to adopt the proposal by some commenters that price should be the "default" presumptive determinant of winning bids. Therefore, to the extent that Commission may decide to adopt such a proposal, Hayes would urge the Commission to consider adopting a separate bidding requirement for eligible and ineligible services to avoid this type of pricing arbitrage that almost certainty would occur.

no state or local competitive bidding process is available to the applicant. Hayes believes, though, that the streamlined competitive bidding process should be as simple as possible so that it does not serve as impediment to qualified schools and libraries who, by their nature, may not have surplus resources to navigate through a complex set of federal requirements that are separate from any applicable state or local procurement laws with which the applicant also must comply.

IV. APPLICATION AND APPEAL PROCESSING TIMEFRAMES WOULD GREATLY IMPROVE THE EFFICIENCY OF E-RATE PROGRAM

Hayes submits that regardless of the results of an E-rate funding decision, if a funding commitment decision letter is issued after the beginning of a school year, as a practical matter, the school may not be able to utilize funding even if it is granted. Indeed, schools and service providers usually are hesitant to move forward on E-rate service contracts when the participants are unsure if E-rate funding will be granted. For example, the school may not have extra funding to cover the cost of E-rate discounts if not granted, or it may not be economically feasible for the service provider to provide service to the school at the discounted prices.

Similarly, long appeal processing times for E-rate applications can prevent a school from utilizing the E-rate funding even if the appeal is ultimately successful and the funding granted. Again, for the same reasons that service may not be initiated while a funding commitment decision is still pending, schools and service providers are usually hesitant to move forward on a service contract when funding appeals are pending, even if the participants believe that they

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[14] *See also* Initial Comments of Ohio SchoolNet Commission at 5 and New York City Department of Education at 3 (suggesting that the applicants be allowed to certify compliance with state and local procurements as a substitute for the Form 470 competitive bidding process).

likely will prevail on the appeal. Additionally, in the case of multi-year contracts, even if the school and service provider moved forward on the service contract, if the appeal is still pending by the next filing window, the school usually is forced to expend additional resources to re-bid the services due to the uncertainty of funding under the multi-year contract.

Moreover, the practical result of lengthy processing times for E-rate applications and appeals is that the schools involved in these situations are not able to utilize funding, even if the funding is ultimately granted. This result is contrary to the basic, and most important, purpose of the E-rate program -- enabling qualified schools and libraries to obtain affordable telecommunications and Internet access services. Hayes submits that a maximum six-month processing deadline for all E-rate applications and appeals is a reasonable processing timeframe to which the FCC and USAC should commit. Such a processing deadline would greatly assist in the utilization of E-rate funding by successful E-rate applicants, as well as the overall efficiency of the entire program that is currently being weighed down by long processing delays.

V. APPLICANTS WHO RELY ON DELAYED STATE OR LOCAL BUDGET PROCESSES SHOULD BE ALLOWED TO DEFER GUARANTEE OF "MATCHING" FUNDS AS A CONDITION OF FUNDING GRANT

Under the current E-rate rules, applicants must demonstrate that they have sufficient "matching" funds to pay the undiscounted portion of their funding request.[15] It is not uncommon, however, for applicants that rely on funding from state governments to not have received their funding commitments from the state legislature by the time the E-rate applications are due in February. Some state legislatures do not finalize their budgets until much later in the

year, well after the "matching" fund certification must be submitted as part of the school's E-rate application. The timing of these budget discussions, of course, is typically not within the control of the applicant. As such, applicants in this situation technically would not be able to guarantee "matching" funds for the undiscounted portion of their requests due to circumstances beyond their control.

Hayes submits that the Commission should clarify its rules so that an E-rate applicant who relies on funding from state or local governments is not required to demonstrate the ability to pay matching funds for the undiscounted portion of its E-rate funding request if the applicant has not yet received that year's funding commitment from its state or local legislatures. Instead, as part of the application process, the applicant could be expected to provide a reasonable estimate of the state or local funding that the applicant expects to receive. Then, if granted, the E-rate funding commitment could be conditioned on the state or local authority's authorization of funding necessary to pay the entire undiscounted portion of its granted funding request. Hayes believes this would be a reasonable solution to the predicament currently faced by applicants in this situation. Under this proposal, the Commission and USAC are provided assurances that the undiscounted portion will be paid, while at the same time applicants that rely on state and local funding distributed after February would be allowed to participate in the E-rate program.

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[15] *See Federal-State Joint Board on Universal Service*, CC Docket 96-45, Report and Order, 12 FCC Rcd 8776, ¶¶ 493 (citing *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Recommended Decision, 12 FCC Rcd 87, ¶ 549 (1996)); *see also* http://www.sl.universalservice.org/reference/obligation.asp.

VI. CONCLUSION

For the reasons discussed above, Hayes urges the Commission to adopt an order consistent with the proposals outlined herein.

Respectfully submitted,

/s/

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Date: April 12, 2004

CERTIFICATE OF SERVICE

I, Wendy M. Creeden, hereby certify that on this 12th day of April, 2004, a true and correct copy of the foregoing ***Reply Comments of Hayes E-Government Resources, Inc. in CC Docket No. 02-06*** was sent by via electronic mail to the following:

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